

Office of the State Auditor
Division of State Audit

North Dakota Potato Council
Grand Forks, North Dakota

Audit Report for the Two-Year
Period Ended June 30, 2006
Client Code 61000

Robert R. Peterson
State Auditor



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October 5, 2006

Honorable John Hoeven, Governor

Members of the Legislative Assembly

Diane Peycke, Executive Director
North Dakota Potato Council

Transmitted herewith is the special-purpose financial statement audit of the North Dakota Potato Council for the two-year period ended June 30, 2006. The Office of the State Auditor has the statutory authority to determine the contents of state agency audit reports. The Office of the State Auditor worked with the Legislative Council and the Office of Management and Budget (OMB) to develop the contents of this audit report. The primary goal was to provide the Legislative Audit and Fiscal Review Committee, other legislators and state officials with the information they need to monitor the fiscal affairs of state agencies.

The review of the North Dakota Potato Council's internal control and compliance with laws and regulations governing the agency disclosed three reportable conditions concerning segregation of duties and compliance as shown on page 9 and 12 of this report.

The Office of the State Auditor would like to thank the North Dakota Potato Council and Diane Peycke, its Executive Director for the cooperation we received during our audit.

Sincerely,

Robert R. Peterson
State Auditor

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INDEPENDENT AUDITOR'S REPORT

Honorable John Hoeven, Governor

Members of the Legislative Assembly

Diane Peycke, Executive Director
North Dakota Potato Council

We have audited the special-purpose statements of revenues and expenditures of the North Dakota Potato Council for the two-year periods ended June 30, 2006 and 2004. These financial statements are the responsibility of the management of the North Dakota Potato Council. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards, and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statement is free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statement. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

The accompanying special-purpose financial statements were prepared to provide state decision makers, including the Legislative Audit and Fiscal Review Committee, with a comprehensive overview of the North Dakota Potato Council's operations. The revenues and expenditures are reported as discussed in the first note to the financial statements. These special-purpose financial statements are not intended to be a presentation in conformity with generally accepted accounting principles.

In our opinion, the special-purpose financial statements referred to above presents fairly, in all material respects, the revenues and expenditures of the North Dakota Potato Council for the two-year periods ended June 30, 2006 and 2004, in conformity with the basis of accounting described in the first note to the financial statements.

Our audits were made for the purpose of forming an opinion on the special-purpose financial statements taken as a whole. The statement subsequent to the notes is presented for purposes of additional analysis and is not a required part of the special-purpose financial statements of the North Dakota Potato Council. The statement subsequent to the notes has been subjected to the auditing procedures applied in the audits of the special-purpose financial statements and

in our opinion, is fairly stated in all material respects in relation to the financial statements taken as a whole.

In accordance with *Government Auditing Standards*, we have also issued our report dated October 5, 2006 on our consideration of the North Dakota Potato Council's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants.

This report is intended solely for the information of the Governor, Legislative Audit and Fiscal Review Committee and management of the North Dakota Potato Council and should not be used for any other purpose. However, this report is a matter of public record and its distribution is not limited.

Robert R. Peterson
State Auditor

October 5, 2006

COMPARATIVE STATEMENT OF REVENUES AND EXPENDITURES
For The Two-Year Periods Ended June 30, 2006 and 2004

	Fiscal Years 2006-2005	Fiscal Years 2004-2003
REVENUES:		
Potato Assessments (net of refunds of \$165,195 and \$214,442)	\$ 1,056,723	\$ 951,205
Interest on Investments	1,551	3,537
Total Revenues	<u>\$ 1,058,274</u>	<u>\$ 954,742</u>
EXPENDITURES:		
Operating Expenses	\$ 10,603	\$ 12,927
Contract Payments	953,375	1,127,600
Total Expenditures	<u>\$ 963,978</u>	<u>\$ 1,140,527</u>
Revenue Over/(Under) Expenditures	<u>\$ 94,296</u>	<u>\$ (185,785)</u>

NOTES TO THE SPECIAL-PURPOSE FINANCIAL STATEMENT
For The Two-Year Periods Ended June 30, 2006 and 2004

Note 1 - Summary of Significant Accounting Policies

The responsibility for the financial statement, the internal control structure, and compliance with laws and regulations belongs to the management of the North Dakota Potato Council (Council). A summary of the significant accounting policies follows:

A. Reporting Entity

For financial reporting purposes, the Council includes all funds, programs, and activities over which it is financially accountable. The Council does not have any component units as defined by the Government Accounting Standards Board. The Council is part of the state of North Dakota as a reporting entity. The financial statement reports all expenditure activity of the Council.

The Council was established by section 4-10.1-02 of the North Dakota Century Code for the purpose and objectives of contributing to the stabilization and improvement of the agricultural economy of the state...it being the intended purpose of this chapter that the council through research and advertising shall promote North Dakota grown Irish potatoes. Section 4-10.1-08 provides that the Council shall have the following powers and duties to:

1. Contact and cooperate with any person or agency for research, education, publicity, promotion, and transportation;
2. Expend the funds collected and appropriated for its administration;
3. Employ and prescribe the duties of such personnel as it may deem necessary;
4. Accept donations for council objectives; and
5. Investigate and prosecute to enforce the payment of taxes authorized by this chapter.

Section 4-10.1-09 provides for an assessment on all potatoes grown in the state or sold to a designated handler. All moneys levied and collected under this chapter shall be paid to the Council for deposit in the state treasury to the credit of a fund designated as the "spud fund."

B. Reporting Structure

The financial statement includes all activities of the reporting entity as defined above. These activities are funded from a special revenue fund, fund 220 (the Spud Fund). The statement of revenues and expenditures is a combined statement to give the users an overview of the agency's activity.

C. Basis of Accounting

Revenues and expenditures on the statement of revenues and expenditures are principally reported on the modified accrual basis of accounting, which are generally accepted accounting principles (GAAP) for governmental fund types.

Under the modified accrual basis of accounting revenues are recognized when susceptible to accrual (i.e., measurable and available). Measurable means the amount can be determined,

available means due and collectible within the current period or soon enough thereafter to be used to pay liabilities of the current period. Revenues are considered available if they are collected within 30 days after fiscal year-end. Expenditures are recorded when goods or services are received. Exceptions include principle and interest expenditures that are recorded when due, compensated absences that are recorded when paid, and claims and judgments.

As stated above, there can be differences between revenues and expenditures reported on the state's accounting system and budget basis and those reported by the Office of Management and Budget in the state's CAFR in accordance with GAAP. Basically there are two types of differences, accounting and statutory.

Accounting differences can include:

- A. Loan receipts and loan disbursements are accounted for as revenues and expenditures on the state's accounting system (and at times are budgeted as expenditures).
- B. Revenue reported on the statement of revenues and expenditures can differ from GAAP revenues because certain receivables are accrued for GAAP purposes while they were not recorded as revenue on the state's accounting system when they are received after the apply-back period.
- C. Certain transfers are recorded as revenues and expenditures on the state's accounting system.
- D. Expenditures recorded on the state's accounting system do not report expenditures relating to capital lease and other financing arrangements.

Statutory differences can occur because of North Dakota Century Code section 54-44.1-11. This section requires the Office of Management and Budget to cancel most unexpended appropriations 30 days after the end of each biennial period. Certain GAAP expenditures are not recorded as budgetary expenditures because the agency does not have the ability to pay the expenditures within 30 days after the end of the biennium. These are relatively rare occurrences, and when significant, will be clearly disclosed.

D. Other GAAP Reporting Differences

GAAP financial statements would include a balance sheet by fund type and account group. Revenues, expenditures, and expenses would also be reported by fund type. GAAP financial statements would also provide more complete note disclosures. This type of information is available in the state's comprehensive annual financial report and the Office of Management and Budget's combining statements by department.

For this report, revenues and expenditures are reported on a departmental basis to give an overview of the Council's operations. All revenues and expenditures are included regardless of the nature of the activities (proprietary fund types are included with governmental fund types when applicable).

Note 2 - Related Parties

The Red River Valley Potato Growers Association (RRVPGA) located in East Grand Forks, Minnesota, is a related party of the Council. The RRVPGA is under contract with the Council to provide promotion, advertising, research, and development of Irish potatoes grown in North Dakota. The amount paid under contract was \$450,000, \$475,000, and \$550,000 for each fiscal year ended June 30, 2006, 2005, and 2004, respectively.

The Executive Director of the Council, who performs all the administrative duties of the Council, is under contract with the Council as an independent contractor, not as a state employee. Under the contract, the Executive Director was paid \$14,150 for each fiscal year 2006 and 2005, and \$13,800 for each fiscal year 2004 and 2003. The Executive Director also performs the administrative duties for the RRVPGA and for a region of the Minnesota Potato Council.

Note 3 - Other Significant Items

The Council's deposits and investments at June 30, 2006 were \$143,431 and \$6,957 and at June 30, 2004, were \$14,505 and \$6,772, respectively. These amounts represent approximately 4 months of expenditures.

North Dakota Century Code 4-10.1-09 states the Council shall levy an assessment of two cents per hundredweight on all potatoes grown in the state or sold to a designated handler. The Council may increase the assessment by not more than one-half cent per hundredweight per year until a maximum assessment of four cents per hundredweight is reached.

The Council has chosen to assess potatoes at three cents per hundredweight during fiscal years 2006, 2005, 2004, and 2003.

RESPONSES TO LAFRC AUDIT QUESTIONS

The Legislative Audit and Fiscal Review Committee (LAFRC) requests that certain items be addressed by auditors performing audits of state agencies.

1. What type of opinion was issued on the financial statements?

Unqualified.

2. Was there compliance with statutes, laws, rules, and regulations under which the agency was created and is functioning?

Yes.

3. Was internal control adequate and functioning effectively?

No. One person maintains the North Dakota Potato Council's records, therefore there is a lack of segregation of duties and the internal control system is very limited. No recommendation will be made since it is not feasible for the North Dakota Potato Council to implement further segregation.

4. Were there any indications of lack of efficiency in financial operations and management of the agency?

No.

5. Has action been taken on findings and recommendations included in prior audit reports?

No. Many of the issues from prior audits were resolved and much improvement has been made, however we still noted issues dealing with timely submission and accuracy of closing packages (See page 12) and timely payments (See page 12).

6. Was a management letter issued? If so, provide a summary below, including any recommendations and the management responses.

Yes, a management letter was issued and is included on page 13 of this report, along with management's response.

LAFRC AUDIT COMMUNICATIONS

1. *Identify any significant changes in accounting policies, any management conflicts of interest, any contingent liabilities, or any significant unusual transactions.*

There were no significant changes in accounting policies, no management conflicts of interest were noted, no contingent liabilities were identified, or significant unusual transactions.

2. *Identify any significant accounting estimates, the process used by management to formulate the accounting estimates, and the basis for the auditor's conclusions regarding the reasonableness of those estimates.*

The North Dakota Potato Council's financial statement does not include any significant accounting estimates.

3. *Identify any significant audit adjustments.*

None.

4. *Identify any disagreements with management, whether or not resolved to the auditor's satisfaction relating to a financial accounting, reporting, or auditing matter that could be significant to the financial statements.*

None.

5. *Identify any serious difficulties encountered in performing the audit.*

None.

6. *Identify any major issues discussed with management prior to retention.*

This is not applicable for audits conducted by the Office of the State Auditor.

7. *Identify any management consultations with other accountants about auditing and accounting matters.*

None.

8. *Identify any high-risk information technology systems critical to operations based on the auditor's overall assessment of the importance of the system to the agency and its mission, or whether any exceptions identified in the six audit report questions to be addressed by the auditors are directly related to the operations of an information technology system.*

ConnectND Finance is a high-risk information technology system critical to the North Dakota Potato Council.

**REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON
COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF SPECIAL-PURPOSE
FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH
GOVERNMENT AUDITING STANDARDS**

Honorable John Hoeven, Governor

Members of the Legislative Assembly

Diane Peycke, Executive Director
North Dakota Dry Bean Council

We have audited the special-purpose financial statement of the governmental activities and the major fund of the North Dakota Potato Council as of and for the two-year period ended June 30, 2006, and have issued our report thereon dated October 5, 2006. We conducted our audit in accordance with auditing standards generally accepted in the United States of America, and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered North Dakota Potato Council's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statement and not to provide assurance on the internal control over financial reporting. However, we noted one matter involving the internal control over financial reporting and its operation that we consider to be a reportable condition. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect North Dakota Potato Council's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. The reportable condition noted above is that there is no segregation of duties. However, no finding will be separately reported, as it is not feasible to obtain proper segregation of duties due to the size of this entity.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial

reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe the reportable condition described above is a material weakness. We also noted other matters involving the internal control over financial reporting that we have included in the Management Letter on page 13 of this report.

Compliance

As part of obtaining reasonable assurance about whether North Dakota Potato Council's financial statement is free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed two instances of noncompliance that are included in the Prior Audit Findings on page 12 of this report and the Management Letter on page 13 reported under *Government Auditing Standards*.

This report is intended solely for the information of the Governor, Legislative Audit and Fiscal Review Committee, and management of the North Dakota Potato Council and is not intended to be and should not be used by anyone other than these specified parties.

Robert R. Peterson
State Auditor

October 5, 2006

DETAILED COMPARATIVE STATEMENT OF REVENUES AND EXPENDITURES

Departmental Information**For The Two-Year Periods Ended June 30, 2006 and 2004**

	Fiscal Years 2006-2005	Fiscal Years 2004-2003
REVENUES:		
Potato Assessments (net of refunds of \$165,195 and \$214,442	\$ 1,056,723	\$ 951,205
Interest on Investments	1,551	3,537
Total Revenues	<u>\$ 1,058,274</u>	<u>\$ 954,742</u>
EXPENDITURES:		
Travel	\$ 35	\$ 1,536
Office Supplies	600	553
Mailing Services	104	
Postage and P.O. Box Renta	759	1,275
Liability Insurance	780	1,564
Telephone & Telegraph - Non IT	1,885	1,980
Conference Expenses	637	
Stipends	1,075	725
Misc. Contractual Fees	953,375	1,127,600
Audit	4,397	4,170
Legal	331	854
Repairs		270
Total Expenditures	<u>963,978</u>	<u>1,140,527</u>
Revenue Over/(Under) Expenditures	<u>\$ 94,296</u>	<u>\$ (185,785)</u>

Note: Some numbers from FY04-03 were reclassified in order to make the two audit periods more comparable.

FY04-03 Professional Services = Audit + Legal

FY04-03 Utilities = Telephone & Telegraph-Non IT

FY04-03 Dues and Professional Development = Stipends

STATUS OF PRIOR AUDIT FINDINGS
For The Two-Year Periods Ended June 30, 2006 and 2004

Timely Submission and Accuracy of Closing Packages (Prior Audit Finding #1)

In the past audit we noted that closing packages were submitted late to OMB. Also, incorrect amounts were submitted.

RECOMMENDATION:

We recommended that the Council prepare accurate and timely closing packages in accordance with OMB policy 200 and thereby properly report activity in accordance with generally accepted accounting principles.

STATUS: Not Implemented.

We noticed three closing packages were late and two were inaccurate or incomplete. Four of these were for fiscal year 2005 and one for fiscal year 2006.

RESPONSE:

The Executive Director acknowledges the recommendation and will comply with the auditor recommendations.

Non-Compliance with Contract Terms and Conditions-Timely Payments
(Prior Audit Finding #2)

In the past audit we noted that payments made by the council were not made in a timely manner. The council was behind on contract payments as well as paying late fees on other late bills.

RECOMMENDATION:

We recommended that the executive director make payments in a timely manner.

STATUS: Not Implemented.

The contract between the executive director and the Potato council specified that contract payments are to be made on the last day of each month. No payments were made on the last day of the month during either fiscal year 2005 or 2006.

RESPONSE:

The Executive Director acknowledges the recommendation from the auditor and will comply with the recommendation in the future.

Management Letter (Informal Recommendations)

October 5, 2006

Ms. Diane Peycke, Executive Director
North Dakota Potato Council
PO Box 5674
Grand Forks, ND 58206

Dear Ms. Peycke:

We have performed an audit of the North Dakota Potato Council for the two-period ended June 30, 2006, and have issued a report thereon. As part of our audit, we gained an understanding of the North Dakota Potato Council's internal control structure to the extent we considered necessary to achieve our audit objectives. We also performed tests of compliance as described in the same report.

Our audit procedures are designed primarily to enable us to report on our objectives including those related to internal control and compliance with laws and regulations and may not bring to light all weaknesses in systems and procedures or noncompliance with laws and regulations which may exist. We aim, however, to use our knowledge of your organization gained during our work to make comments and suggestions which we hope will be useful to you.

In connection with the audit, gaining an understanding of the internal control structure, and tests of compliance with laws and regulations referred to above, we noted certain conditions we did not consider reportable within the context of your audit report. These conditions relate to areas of general business practice or control issues that have no significant bearing on the administration of North Dakota Potato Council funds. We do, however, want to present our recommendations to you for your consideration and whatever follow-up action you consider appropriate. During the next audit we will determine if these recommendations have been implemented, and if not, we will reconsider their status as non-reportable conditions.

The following present our informal recommendations.

Non-Current List of Designated Handlers

Informal Recommendation 06-1:

The list provided of designated handlers was not accurate, complete, and up-to-date. Seven out of twenty of designated handlers selected for testing were no longer growing potatoes.

- Keep a current and complete list of designated handlers.

North Dakota Potato Council's Response:

The executive director gave the wrong list of handlers to the auditor due to a computer error. The executive director has an updated list that she updates each quarter so handlers on the list the auditor had that weren't growing potatoes any longer were not getting the current quarterly reports. The executive director acknowledges the error and will make sure the correct list is given to the auditor in the future.

Improper Account Coding**Informal Recommendation 06-2:**

Non-employee travel was coded wrongly to conference expense, a contract payment was coded as a reduction of revenue instead of as an expenditure, and a transfer fee was incorrectly coded as a misc. contractual fee.

- Ensure proper use of account codes and take more care to ensure all entries are coded properly.

North Dakota Potato Council's Response:

The executive director acknowledges the recommendation and will familiarize herself with the PeopleSoft accounting system.

Non-Compliance with Contract Terms and Conditions**Informal Recommendation 06-3:**

Payment guidelines according to contract terms were not followed. The NPPGA was paid fees that exceeded quarterly maximums as defined in contract terms.

- Ensure contract terms and conditions are followed, and
- Ensure payments are made for proper amounts specified in the contract terms.

North Dakota Potato Council's Response:

The executive director acknowledges the recommendation by the auditor and will comply in the future.

I encourage you to call me at 239-7289 if you have any questions about the implementation of recommendations included in your audit report or this letter.

Sincerely,

John Grettum, CPA
Audit Manager